ECORD
AND
RIEFS

FILED
AUG 31 2017
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 15-1439

In the
Supreme Court of the United States

CYAN, INC., ET AL.,

Petitioners,

v.

BEAVER COUNTY EMPLOYEES RETIREMENT FUND, ET AL.

Respondents.

On Writ of Certiorari to the Court of Appeal of the State of California, First Appellate District

---

BRIEF FOR DRI – THE VOICE OF THE DEFENSE BAR AS *AMICUS CURIAE* SUPPORTING PETITIONERS

JOHN E. CUTTINO
President of DRI— The Voice of the Defense Bar
55 W. Monroe St.
Suite 2000
CHICAGO, IL 60603

MARY MASSARON
Counsel of Record
HILARY A. BALLENTINE
PLUNKETT COONEY
38505 Woodward Avenue
Suite 100
Bloomfield Hills, MI 48304
(248) 901-4000
mmassaron@plunkettcooney.com

Counsel for Amicus Curiae DRI – The Voice of the Defense Bar

August 31, 2017

TABLE OF CONTENTS

TABLE OF CONTENTS i

TABLE OF AUTHORITIES iii

STATEMENT OF INTEREST OF *AMICUS CURIAE* 1

SUMMARY OF THE ARGUMENT 4

ARGUMENT 6

I. Through Its Enactment Of The Securities Litigation Uniform Standards Act Of 1998, Congress Intended That "Covered Class Actions" Alleging Only Violations Of The Securities Act Of 1933, Such As The One At Issue, Be Litigated In A Federal Forum Subject To Protective Laws Uniformly Applied 6

A. From 1933 To 1995, Securities Legislation Was Marked By Concurrent Jurisdiction In State And Federal Courts. 7

B. The Number Of Securities Class Actions Filed In State Courts Increased Dramatically As Plaintiffs Sought To Avoid The Protections Granted To Defendants By The Private Securities Litigation Reform Act Of 1995. 8

C. The SLUSA Was Designed To Curb Plaintiffs' Efforts To Circumvent The Protections Of The Reform Act By Making Federal Court The Exclusive Venue For Most Securities Class Action Lawsuits. 12

II. Allowing Plaintiffs To Litigate Covered Class Actions Alleging Only 1933 Act Claims In State Courts, Despite The Plain Command Of The SLUSA That Such Class Actions Be Adjudicated In A Federal Forum, Creates A Host Of Problems For Defendants. 14

CONCLUSION 21

TABLE OF AUTHORITIES

Cases

Ernst & Ernst v. Hochfielder,
425 U.S. 185 (1976) 7

Knox v. Agria Corp.,
613 F. Supp. 2d 419 (S.D.N.Y. 2009) 13

Lander v. Hartford Life & Annuity Ins. Co.,
251 F.3d 101 (2d Cir. 2001) 9

Luther v. Countrywide Fin. Corp.,
195 Cal. App. 4th 789 (2011) 14, 19

Matsushita Elec. Indus. Co. v. Epstein,
516 U.S. 367 (1996) 8

Matter of Rhone-Poulenc Rorer, Inc.,
51 F.3d 1293 (7th Cir. 1995) 18, 20

Merrill Lynch, Pierce, Fenner & Smith Inc v. Dabit,
547 U.S. 71 (2006) 7

Murphy v. Gallagher,
761 F.2d 878 (CA 2 1985) 8

Sand Hill Energy, Inc. v. Ford Motor Co.,
83 S.W.3d 483 (Ky. 2002) (Cooper, J., dissenting), *vacated and remanded* 538 U.S. 408 (2003), *rev'd on remand*, 142 S.W. 2d 153 (Ky. 2004) 17

Thorogood v. Sears, Roebuck and Co.,
547 F.3d 742 (7th Cir. 2008) 18

Rules

Fed. R. Civ. P. 11 11

Fed. R. Civ. P. 11(b) 11

Supreme Court Rule 37.3 1

Supreme Court Rule 37.6 1

Statutes

15 U.S.C. §77*l*(a)(2) 7
15 U.S.C. §77p(b) 13
15 U.S.C. §77p(c) 13
15 U.S.C. §77p(f) 13
15 U.S.C. §77p(f)(2) 5
15 U.S.C. §77(v) 2, 13
15 U.S.C. §77z-1 8
15 U.S.C. §77z-1(a)(3)(B) 10
15 U.S.C. §77z-1(b) 10
15 U.S.C. §77z-2(c)(1)(A)(i) 5
15 U.S.C. §78aa(a) 8
15 U.S.C. §78u 8
15 U.S.C. §78u-4(b) 5
15 U.S.C. §78u-4(b)(3)(B) 10
15 U.S.C. §78u-4(c) 11
15 U.S.C. §78u-5(c)(1)(A)(i) 5
15.U.S.C. §78u-4(b)(3)(B) 10
28 U.S.C. § 1441(a) 7
Class Action Fairness Act 5
Private Securities Litigation Reform Act of 1995 . 2, 4, 5, 6, 8, 9, 10, 11, 12, 13, 15, 17, 18, 19, 20
Securities Act of 1933 . 2, 3, 4, 5, 6, 7, 8, 10, 11, 12, 13, 14, 20
Securities Exchange Act of 1934 ..... 4, 8, 10, 11
Securities Litigation Uniform Standards Act of 1998 ..... 2, 3, 5, 6, 12, 13, 14, 17, 19, 20

Legislative Materials

H.R. Conf. Rep. No. 104-369 (1995) 4, 5, 9, 10

H.R. Conf. Rep. No. 105-803 (1998) 9

H.R. Rep. No. 105-640 (1998) 11, 12, 14

Joint prepared statement of Joseph A. Grundfest and Michael A. Perino, "Reform Act Hearing," July 24, 1997 12

S. Rep. No. 104-98 (1995) 4, 9, 17, 19

S. Rep. No. 105-182 (1998) 11, 12

S. Rep. No. 109-14 (2005) 6

S. Rep. No. 109-15 (2005) 20

Statement of Senator Pete Domenici, Hearing on Securities Litigation Reform Proposals, Subcommittee on Securities, Senate Committee on Banking, Housing and Urban Affairs, March 2, 1995 4

Testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission Concerning The Impact Of The Private Securities Litigation Reform Act of 1995 Before The Subcommittee on Securities, Committee on Banking, Housing, and Urban Affairs, July 24, 1997, 1997 WL 418051 ... 19

Miscellaneous

American Tort Reform Association, *Judicial Hellholes 2006*, http://www.atra.org/reports/hellholes/ 15

Asbestos for Lunch, Panel Discussion at the Prudential Securities Financial Research and Regulatory Conference (May 9, 2002), *in* INDUSTRY

COMMENTARY (Prudential Securities, Inc., N.Y., New York) June 11, 2002 15

Barry F. McNiel, et al., *Mass Torts and Class Actions: Facing Increased Scrutiny*, 167 F.R.D. 483 (updated 8/5/96) 18

Bradley J. Bondi, *Facilitating Economic Recovery and Sustainable Growth Through Reform of the Securities Class-Action System: Exploring Arbitration as an Alternative to Litigation*, 33 Harv. J.L. & Pub. Pol'y 607 (Spring 2010) 20

Henry J. Friendly, Federal Jurisdiction: A General View 120 (1973) 20

James Bohn & Stephen Choi, *Fraud in the New-Issues Market: Empirical Evidence on Securities Class Actions*, 144 U. Pa. L. Rev. 903, 970 (1996) 21

Michael B. Barnett, *The Plaintiffs' Bar Cannot Enforce the Laws: Individual Reliance Issues Prevent Consumer Protection Classes in the Eighth Circuit*, 75 Mo. L. Rev. 207, 208 (Winter 2010) 20

Richard A. Nagareda, *Class Certification in the Age of Aggregate Proof*, 84 N.Y. U. L. REV. 97 (2009) . 18

Robert G. Bone & David S. Evans, *Class Certification and the Substantive Merits*, 51 Duke L.J. 1251 (2002) 18

Thomas E. Willging & Shannon R. Wheatman, *Attorney Choice of Forum in Class Action Litigation: What Difference Does It Make?*, 81 Notre Dame L. Rev. 591 (2006) 18

STATEMENT OF INTEREST OF *AMICUS CURIAE*[1]

Amicus curiae DRI – The Voice of the Defense Bar, is an international organization of more than 22,000 attorneys involved in the defense of civil litigation. DRI is committed to enhancing the skills, effectiveness, and professionalism of defense attorneys. Because of this commitment, DRI seeks to promote the role of defense attorneys, to address issues germane to defense attorneys and their clients, and to improve the civil justice system. DRI has long participated in the ongoing effort to make the civil justice system fairer, more consistent, and more efficient. See http://www.dri.org/About. To promote these objectives, DRI participates as amicus curiae in cases that raise issues important to its membership, their clients, and the judicial system. This is one of those cases.

DRI's interest in this case stems from its members' extensive involvement in civil litigation, including securities class actions. DRI's members are regularly called upon to defend their clients in lawsuits brought pursuant to federal securities laws, which contain a number of protections to curb systemic abuses by plaintiffs. If the decision below is affirmed, however, plaintiffs will continue to bring

---

[1] Pursuant to Supreme Court Rule 37.6, amicus curiae states that no counsel for any party authored this brief in whole or in part and that no entity or person, aside from amicus curiae, its members, and its counsel, made any monetary contribution towards the preparation and submission of this brief. Pursuant to Supreme Court Rule 37.3, counsel of record for all parties has consented to this filing.

and litigate class actions for claimed violations of the Securities Act of 1933 in state courts, where federal protections are not uniformly enforced and applied. No doubt, a decision that follows the rationale of the Superior Court of the State of California, County of San Francisco ("Superior Court") will result in a further increase in the filing of "strike suits" – meritless suits brought to coerce an expensive settlement – in state courts.

DRI has a strong interest in ensuring that the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), which eliminated state-court jurisdiction over "covered class actions" raising only 1933 Act claims, is strictly enforced pursuant to its plain terms. 15 U.S.C. §77(v). The very intent of the SLUSA was to eliminate the federal-to-state-court shift observed after the Private Securities Litigation Reform Act of 1995 was enacted and plaintiffs flocked to state courts to avoid the Reform Act's heightened pleading requirements. Yet the decision below effectively nullifies a portion of the SLUSA by allowing plaintiffs to maintain these class actions in state court and circumvent the federal rules. This threatens to open the floodgates of litigation in derogation of the Legislature's intent to eliminate state court jurisdiction of large class actions alleging only 1933 Act claims. This, in turn, directly affects the fair, efficient, and consistent functioning of our civil justice system and, as such, it is of vital interest to the members of DRI.

DRI has a unique vantage point to help this Court understand the importance of proper adherence to the outer bounds of state courts'

jurisdiction over securities class actions, not only from a legal standpoint, but also from practical and economic standpoints as well. DRI, alone and in conjunction with other legal organizations, has conducted seminars studying these lawsuits long before this case. DRI has also compiled a Class Action Compendium designed to provide civil defense lawyers and corporate counsel with an understanding of the intricacies of class action practice and procedure. These and other seminars and writings on class action litigation reveal DRI's longstanding interest in mass action litigation and its knowledge about this litigation and its abuses. In seeking to rectify litigation abuses and to improve the civil justice system, DRI has submitted testimony regarding the federal rules of civil procedure, potential legislation relating to class actions, and addressed other issues arising from class action litigation with federal and state legislators, courts, and rule-making bodies.

Based on its members' extensive real-world experience, DRI is uniquely suited to explain why the better approach is to adhere to the SLUSA's clear elimination of state-court jurisdiction over covered class actions alleging only 1933 Act claims and allow those actions to proceed exclusively in a federal forum with securities laws designed to carefully balance the need to protect innocent investors from fraudulent practices with the need to protect innocent defendants from meritless, yet costly, lawsuits.

SUMMARY OF THE ARGUMENT

"The private securities litigation system is too important to the integrity of American capital markets to allow this system to be undermined by those who seek to line their own pockets by bringing abusive and meritless suits." H.R. Conf. Rep. No. 104-369, 31 (1995). It is for this precise reason that Congress has enacted a number of federal securities laws to balance the competing concerns of protecting investors against fraud while curtailing extortionist settlements from innocent defendants.

One of those laws was the Private Securities Litigation Reform Act of 1995, which, as a co-sponsor succinctly summarized, was intended to "return some fairness and common sense to our broken securities class action litigation system, while continuing to provide the highest level of protection to investors in our capital markets." S. Rep. No. 104-98,4 (1995), quoting Statement of Senator Pete Domenici, Hearing on Securities Litigation Reform Proposals, Subcommittee on Securities, Senate Committee on Banking, Housing and Urban Affairs, March 2, 1995. The Reform Act made several amendments to the Securities Act of 1933 and the Securities Exchange Act of 1934, calling for heightened pleading requirements for private securities fraud actions, certification requirements for lead plaintiffs, and automatic discovery stays during the pendency of a motion to dismiss. It also placed limitations on recoverable damages and attorney's fees, and established a safe-harbor provision for forward-looking statements to insulate defendants from liability. H.R. Conf. Rep. No. 104-369, pp. 42-47

(1995); 15 U.S.C. §77z-2(c)(1)(A)(i), §78u-5(c)(1)(A)(i), §78u-4(b).

Unfortunately for defendants, plaintiffs found a loophole: file their securities suits in state courts in order to avoid the Reform Act's heightened requirements. Like the lawsuit at issue here, the bulk of these suits have been brought in California. Congress responded to this noticeable trend by enacting the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), which amended the Securities Act of 1933 to eliminate state court jurisdiction for "covered class actions" alleging state-law securities claims.

There is no dispute that this case is a "covered class action" – statutorily defined as any damages action on behalf of more than 50 people. 15 U.S.C. §77p(f)(2). Nonetheless, the decision below allowed Respondents' lawsuit, which alleged only violations of the 1933 Act, to proceed in a California state court. In this way, the opinion below threatens to strip the Reform Act of its protections by allowing plaintiffs to litigate covered class actions in state court rather than in a federal forum carefully designed to protect innocent defendants. And clever plaintiffs will not just file in any state court – they will forum shop for "magnet" or "magic" state jurisdictions – certain courts with relaxed rules and hostility to out-of-state defendants. In magnet jurisdictions, "state court judges are less careful than their federal court counterparts about applying the procedural requirements that govern class actions[,]" a phenomenon Congress noted when passing the Class Action Fairness Act (CAFA) in 2005. S. Rep. No. 109-

14, 13-24 (2005). In plaintiff-friendly jurisdictions, securities class actions frequently result in extortionist settlements.

By making federal court the exclusive forum for class actions of this nature, Congress intended that the SLUSA would ensure that the safeguards of the Reform Act are enforced uniformly throughout the country. Yet under the decision below, plaintiffs now have a roadmap to avoid the federal forum and the Reform Act's tailor-made protections for defendants. This, in turn, leads to an increase in "strike suits" brought by "professional plaintiffs," for no other reason than to extract a settlement regardless of the lack of merit of the underlying claims. This contravenes a key purpose of securities legislation for the last eighty-plus years.

ARGUMENT

I. Through Its Enactment Of The Securities Litigation Uniform Standards Act Of 1998, Congress Intended That "Covered Class Actions" Alleging Only Violations Of The Securities Act Of 1933, Such As The One At Issue, Be Litigated In A Federal Forum Subject To Protective Laws Uniformly Applied.

The historical framework of securities legislation, from the Securities Act of 1933 to the Securities Litigation Uniform Standards Act of 1998, evidences a legislative intent to curb abuses attendant with securities class action litigation, and culminates in a statutory requirement that certain class actions, such as the one at issue here, be litigated in a federal forum governed by protective laws that are consistently applied.

A. From 1933 To 1995, Securities Legislation Was Marked By Concurrent Jurisdiction In State And Federal Courts.

Out of the Stock Market Crash of 1929 arose the Securities Act of 1933 ("1993 Act" or "Act"), legislation "designed to provide investors with full disclosure of material information concerning public offerings[.]" *Ernst & Ernst v. Hochfielder*, 425 U.S. 185, 195 (1976); *Merrill Lynch, Pierce, Fenner & Smith Inc v. Dabit*, 547 U.S. 71, 78 (2006). "[P]rimarily concerned with the regulation of new offerings[,]" the 1933 Act created a cause of action for false statements made in connection with the public offering of stocks. 15 U.S.C. §77*l*(a)(2). Section 22(a) of the 1933 Act provided for concurrent jurisdiction in both state and federal courts over claims arising under the Act. Section 22(a) also expressly stated that claims brought in state court were not subject to removal to federal court: "[N]o case arising under this subchapter and brought in any State court of competent jurisdiction shall be removed to any court of the United States." *Id.* In practice, Section 22(a)'s non-removal provision worked to preclude cases brought in state court under the 1933 Act from being removed to federal court under 28 U.S.C. § 1441(a) (providing for a defendant's removal to federal court "any civil action brought in a State court of which the district courts of the United States have original jurisdiction" unless "as otherwise provided by an Act of Congress[.]").

Investors were granted further protections from fraud transpiring in the securities exchange setting through Congress' enactment of the Securities

Exchange Act of 1934 ("1934 Act"). While the 1934 Act provided for broader regulations than the 1933 Act, the 1934 Act granted federal courts "exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder." 15 U.S.C. §78aa(a). While "[t]he legislative history of the Exchange Act elucidates no specific purpose on the part of Congress" in conferring exclusive federal jurisdiction, *Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367, 383 (1996), Congress sought "'to achieve greater uniformity of construction and more effective and expert application of that law.'" *Id.*, quoting *Murphy v. Gallagher*, 761 F.2d 878, 885 (CA 2 1985).

In light of the 1933 Act and the 1934 Act, securities regulation and litigation was marked by a dual federal-state framework. That all changed, however, after Congress' passage of the Private Securities Litigation Reform Act of 1995 ("Reform Act") (codified in part at 15 U.S.C. §77z-1, §78u).

B. The Number Of Securities Class Actions Filed In State Courts Increased Dramatically As Plaintiffs Sought To Avoid The Protections Granted To Defendants By The Private Securities Litigation Reform Act Of 1995.

The Reform Act was aimed at curbing a number of abusive practices by plaintiffs in securities class action litigation. The drafters of the Reform Act hoped that it would "promote uniformity in the securities market" by preventing "'strike suits' –

meritless class actions that allege fraud in the sale of securities." *Lander v. Hartford Life & Annuity Ins. Co.*, 251 F.3d 101, 107 (2d Cir. 2001), citing H.R. Conf. Rep. No. 105-803 (1998). As the Senate Committee on Banking, Housing, and Urban Affairs noted, oftentimes these strike suits are "based on nothing more than a company's announcement of bad news, not evidence of fraud." S. Rep. No. 104-98, 4 (1995). Yet they "increase the cost of raising capital and chill corporate disclosure[.]" *Id.* And defending strike suits often forces defendants into settlement of even meritless claims. H.R. Conf. Rep. No. 104-369 (1995).

The Reform Act also sought to address abuses triggered by the emergence of "professional plaintiffs" – individuals who repeatedly appear as lead plaintiffs in securities class action lawsuits for no reason other than to receive "bounty payment or bonuses." *Id.* at 32-33. Those individuals, a House Conference Committee Report aptly reasoned, should not be permitted to act as lead plaintiffs:

> The Conference Committee believes these practices have encouraged the filing of abusive cases. Lead plaintiffs are not entitled to a bounty for their services. Individuals who are motivated by the payment of a bounty or bonus should not be permitted to serve as lead plaintiffs. These individuals do not adequately represent other shareholders-in many cases the "lead plaintiff" has not even read the complaint.

Id. at 33.

The legislature attempted to cure this problem by adding several new sections to the 1933 and 1934 Acts. First, the Reform Act required a lead plaintiff to file a sworn statement with the complaint certifying, among other things, that he or she (1) reviewed and authorized the filing of the complaint, (2) did not purchase the securities at the direction of counsel in order to participate in the lawsuit, and (3) is willing to serve as the lead plaintiff on behalf of the class. 15 U.S.C. §77z-1(a)(3)(B). The Reform Act also required that class counsel by retained by the most adequate plaintiff in hopes that "the plaintiff will choose counsel" rather than "counsel choosing the plaintiff." H.R. Conf. Rep. No. 104-369, p 35 (1995).

The Reform Act also addressed "fishing expedition" lawsuits marked by abusive discovery practices. "According to the general counsel of an investment bank, 'discovery costs account for roughly 80% of the total litigation costs in securities fraud cases.'" H.R. Conf. Rep. No. 104-369, p 37 (1995). This, combined with the amount of time key employees are forced to spend to respond to discovery requests, *id.*, led to a new statutory requirement that the courts stay all discovery pending a ruling on a motion to dismiss, except in the exceptional case where particularized discovery was necessary to preserve evidence or to prevent undue prejudice to a party. 15 U.S.C. §77z-1(b), 78u-4(b)(3)(B).

Another key provision of the Reform Act addressed the award of attorney fees to prevailing parties in abusive litigation. Two competing interests were at play here: one, the need to reduce the filing of

meritless securities lawsuits, and two, the ability of victims of fraud to pursue legitimate claims. To balance these concerns, the Reform Act strengthened the sanctions provisions of Fed. R. Civ. P. 11, which require an attorney to conduct a reasonable investigation of the factual and legal basis of his claim before filing. It did so by adding new provisions to the 1933 and 1934 Acts requiring courts to include specific findings in the record at the conclusion of the action regarding whether all parties and all attorneys have complied with each Rule 11(b) requirement. 15 U.S.C. §78u-4(c).

"Prior to the passage of the Reform Act, there was essentially no significant securities class action litigation brought in State court." H.R. Rep. No. 105-640, 10 (1998). But as noted at a July 1997 hearing of the Subcommittee on Securities, the Reform Act caused "a noticeable shift in class action litigation from federal to state courts." S. Rep. No. 105-182, 3 (1997). This shift was characterized by the U.S. Securities and Exchange Commission (SEC) as "'potentially the most significant development in securities litigation' since passage of the Reform Act," H.R. Rep. No. 105-640, 10 (1998), while former SEC Commissioner Joseph Grundfest and another Stanford Law School faculty member summarized the apparent reason for the shift:

> Two phenomena seem to explain the bulk of this shift. First, there appears to be a "substitution effect" whereby plaintiff's counsel file state court complaints when the underlying facts appear not to satisfy new, more stringent federal pleading requirements,

> or otherwise seek to avoid the substantive or procedural provisions of the Act. Second, plaintiffs appear to be resorting to increased parallel state and federal litigation in an effort to avoid federal discovery stays or to establish alternative state court venues for settlement of federal claims.

S. Rep. No. 105-182, 3 (1998), citing Joint prepared statement of Joseph A. Grundfest and Michael A. Perino, "Reform Act Hearing," July 24, 1997, p. 6.

To curtail the proliferation in state courts of securities class actions beyond the reach of the Reform Act's protections, Congress enacted further protective legislation: the Securities Litigation Uniform Standards Act.

C. The SLUSA Was Designed To Curb Plaintiffs' Efforts To Circumvent The Protections Of The Reform Act By Making Federal Court The Exclusive Venue For Most Securities Class Action Lawsuits.

The Securities Litigation Uniform Standards Act (SLUSA) was enacted in 1998 to broadly encourage federal court jurisdiction by making federal court "the exclusive venue for most securities class action lawsuits." H.R. Rep. No. 105-640, pp. 8-9 (1998). Congress designed SLUSA's jurisdictional provisions to "prevent plaintiffs from seeking to evade the protections that Federal law provides against abusive litigation by filing suit in State, rather than in Federal, court." *Id.*, p. 9.

To that end, the SLUSA bars state court jurisdiction over covered class actions that, like this one, only alleged violations of the Securities Act of

1933. 15 U.S.C. §77v. It does so through an exception in the jurisdictional provision of Section 22(a), which exempts "covered class actions" raising 1933 Act claims from concurrent jurisdiction. A covered class action is statutorily defined as a damages action brought on behalf of more than 50 persons. 15 U.S.C. §77p(f). Not only does the SLUSA preclude covered class actions alleging state-law securities claims, see 15 U.S.C. §77p(b), it also permits such precluded class actions to be removed to and dismissed in federal court. 15 U.S.C. §77p(b)-(c).

As one district court aptly explained, under Section 22(a) state courts are no longer courts of competent jurisdiction to hear covered 1933 Act class actions:

> By excluding these covered class actions from concurrent state and federal jurisdiction, federal courts alone have jurisdiction to hear them. After SLUSA, state courts were no longer "court[s] of competent jurisdiction" to hear covered class actions raising 1933 Act claims. Thus, the anti-removal provision does not apply to these covered class actions asserting exclusively federal claims.

Knox v. Agria Corp., 613 F. Supp. 2d 419, 425 (S.D.N.Y. 2009). This interpretation, *Knox* reasoned, "harmonizes with the rest of the SLUSA[,]" including the legislative intent to "prevent certain State private securities class action lawsuits alleging securities fraud from being used to frustrate the objectives of the" Reform Act. *Id.* at 425.

The SLUSA did not foreclose securities lawsuits from proceeding in state court altogether, but rather

preserved a very specific set of state-law actions. These include "(1) actions that are based upon the law of the State in which the issuer of the security in question is incorporated; (2) actions brought by States and political subdivisions, and State pension plans, so long as the plaintiffs are named and have authorized participation in the action; and (3) actions by a party to a contractual agreement (such as an indenture trustee) seeking to enforce provisions of the indenture." H.R. Rep. No. 105-640, p. 9 (1998).

II. Allowing Plaintiffs To Litigate Covered Class Actions Alleging Only 1933 Act Claims In State Courts, Despite The Plain Command Of The SLUSA That Such Class Actions Be Adjudicated In A Federal Forum, Creates A Host Of Problems For Defendants.

The decision below incorrectly concludes that the SLUSA continued state-court jurisdiction over class actions under the 1933 Act. The sole state appellate decision on this issue, *Luther v. Countrywide Fin. Corp.*, 195 Cal. App. 4th 789 (2011), announced that "concurrent jurisdiction of this case survived the amendments to the 1933 Act" and that, contrary to the SLUSA's clear statutory language and the legislative intent, state courts retain concurrent jurisdiction over class actions alleging only 1933 Act claims. *Id.* at 797. The decision in this case follows the reasoning of *Luther* and permits Respondents to proceed with their 1933 Act claim in California's trial court.

When plaintiffs are permitted to proceed with class actions alleging 1933 Act claims in state courts, the systemic abuses that prompted Congress to pass

the Reform Act in the first place are put back into play. DRI's members who regularly defend individuals and corporations are forced to litigate in a state forum devoid of the specific protections of the Reform Act. And plaintiffs are oftentimes particularly strategic about the specific state court they choose to file in, searching for "hellhole" or "magic" jurisdictions "where judges systematically apply laws and court procedures in an unfair and unbalanced manner, generally against defendants in civil lawsuits[.]" See generally, American Tort Reform Association, *Judicial Hellholes 2006*, http://www.atra.org/reports/ hellholes/. Such jurisdictions lack the qualities associated with the rule of law. Litigants do not know the rules in advance. The process is fundamentally unfair – and even nonsensical. Verdicts are rendered based on logic that is incomprehensible.

The well-known plaintiff's attorney, Dickie Scruggs, conceded that some jurisdictions are controlled by the plaintiff's bar. *Asbestos for Lunch*, Panel Discussion at the Prudential Securities Financial Research and Regulatory Conference (May 9, 2002), *in* INDUSTRY COMMENTARY (Prudential Securities, Inc., N.Y., New York) June 11, 2002, at 5. In a jurisdiction like that, cases will not be decided on the basis of the law:

> What I call the "magic jurisdiction," [is] where the judiciary is elected with verdict money. The trial lawyers have established relationships with the judges that are elected; they're State Court judges; they're popul[ists]. They've got large populations of voters who

> are in on the deal, they're getting their [piece] in many cases. And so, it's a political force in their jurisdiction, and it's almost impossible to get a fair trial if you're a defendant in some of these places. The plaintiff lawyer walks in there and writes a number on the blackboard, and the first juror meets the last one coming out the door with that amount of money.... These cases are not won in the courtroom. They're won on the back roads long before the case goes to trial. Any lawyer fresh out of law school can walk in there and win the case, so it doesn't matter what the evidence of law is.

Id. As this statement suggests, a "magic jurisdiction" may result from venality and corruption. It may also reflect a populist philosophy – the notion that the purpose of civil litigation is the re-distribution of wealth and that juries, in dispensing "distributive justice", should not be hamstrung by legal rules and technicalities. A dissenting state supreme court justice, joined by two other justices, expressed this understanding of one verdict as a jury's effort to take money from a deep-pocket, out-of-state defendant:

> In its haste to place its imprimatur on this outrageous verdict by a Clay County "runaway" jury and, presumably, to redistribute the wealth of an out-of-state corporation with requisite deep pockets to stimulate the economy of eastern Kentucky, the majority opinion ignores the facts of this case, our own long-standing precedents, and the Equal Protection and Due Process Clauses of the Fourteenth Amendment of the United

States Constitution as interpreted by the United States Supreme Court.

Sand Hill Energy, Inc. v. Ford Motor Co., 83 S.W.3d 483, 501 (Ky. 2002) (Cooper, J., dissenting), *vacated and remanded* 538 U.S. 408 (2003), *rev'd on remand*, 142 S.W. 2d 153 (Ky. 2004).

Congress designed the SLUSA to provide defendants with an impartial federal forum and to curtail the phenomenon of "magnet" state court jurisdictions, which often certify classes with little to no scrutiny and otherwise prove hostile to out-of-state defendants. The decision below, which DRI anticipates other opportunistic plaintiffs will cite if it is not reversed by this Court, has effectively denied defendants access to the federal courts and resulted in a resurgence of the class-action-friendly state-court magnet jurisdictions whose influence Congress sought to diminish. When defendants are sued in such jurisdictions, defense attorneys are unable to base strategic decisions on the predictability of applying uniform legal standards, given the vagaries of geography and local animus. This leads to another related abuse: forced settlement of even meritless claims.

Exposure in securities fraud class actions is enormous; according to one study noted in conjunction with debate over the Reform Act, the average securities fraud claim was $40 million, with 10% of the cases seeking more than $100 million in damages. S. Rep. No. 104-98, 21. DRI knows all too well the ramifications to defendants nationwide should they be forced to litigate class actions, which would otherwise be confined to federal court, in a

state court. Even in the usual course, "the vast majority of certified class actions settle, most soon after certification." Robert G. Bone & David S. Evans, *Class Certification and the Substantive Merits*, 51 Duke L.J. 1251, 1291-1292 (2002) ("[E]mpirical studies...confirm what most class action lawyers know to be true[.]"); see also Richard A. Nagareda, *Class Certification in the Age of Aggregate Proof*, 84 N.Y. U. L. REV. 97, 99 (2009) ("With vanishingly rare exception, class certification [leads to] settlement, not full-fledged testing of the plaintiffs' case by trial."); Thomas E. Willging & Shannon R. Wheatman, *Attorney Choice of Forum in Class Action Litigation: What Difference Does It Make?*, 81 Notre Dame L. Rev. 591, 647 (2006) ("[A]lmost all certified class actions settle.").

Defendants, unwilling to roll the dice in state court, are placed under intense pressure to settle, even if an adverse judgment seems "improbable." *See Thorogood v. Sears, Roebuck and Co.*, 547 F.3d 742, 745 (7th Cir. 2008); *Matter of Rhone-Poulenc Rorer, Inc.*, 51 F.3d 1293, 1298 (7th Cir. 1995); *see also* Barry F. McNiel, et al., *Mass Torts and Class Actions: Facing Increased Scrutiny*, 167 F.R.D. 483, 489-90 (updated 8/5/96). This is particularly true where out-of-state defendants are forced to litigate a securities class action in state courts that are clearly aligned against defendants.

If affirmed by this Court, the opinion below will also encourage another abuse: using a state court case, filed parallel to a federal court case, in an attempt to gain discovery in the state court case for use in the federal court case where the Reform Act's

discovery stay would apply. Then-U.S. SEC Chairman Arthur Levitt testified about this precise abuse in his report to the President and Congress in the months following passage of the Reform Act. *See* Testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission Concerning The Impact Of The Private Securities Litigation Reform Act of 1995 Before The Subcommittee on Securities, Committee on Banking, Housing, and Urban Affairs, July 24, 1997, 1997 WL 418051, at *3. Opportunistic plaintiffs should not be permitted to sidestep the provisions of the Reform Act by bringing their lawsuits in state courts, where the SLUSA, by its plain terms, eliminated state court jurisdiction over such claims. But that is exactly what is occurring, and what will continue to occur, absent a reversal of the decision below.

The decision below harms DRI's individual and corporate clients in yet another, but equally concerning, way. Abusive state-court litigation hinders publicly-held companies from attracting and maintaining qualified board members for fear of being sued, regardless of how well they actually perform. S. Rep. 104-98, p 21. This has a direct negative impact on the performance of a company, and, in turn, can subject the company to further securities lawsuits.

The loophole created in *Luther* and other cases – including this one – denies defendants the impartial federal forum that the SLUSA's jurisdictional provisions were intended to ensure. The strain this places on the individuals and businesses that DRI's members are regularly called on to defend cannot be

overstated. The costs of a major lawsuit can sound the death knell for new companies and those suffering under today's current economic climate. Bradley J. Bondi, *Facilitating Economic Recovery and Sustainable Growth Through Reform of the Securities Class-Action System: Exploring Arbitration as an Alternative to Litigation*, 33 Harv. J.L. & Pub. Pol'y 607, 612 (Spring 2010). Allowing a covered class action to be brought and litigated in state court gives even more power in upfront settlement discussions to plaintiffs. "Such leverage can essentially force corporate defendants to pay ransom..." S. Rep. 109-15, 17, 20-21 (2005),; Michael B. Barnett, *The Plaintiffs' Bar Cannot Enforce the Laws: Individual Reliance Issues Prevent Consumer Protection Classes in the Eighth Circuit*, 75 Mo. L. Rev. 207, 208 (Winter 2010). This is completely at odds with the very purpose of the Reform Act and the SLUSA. Adopting the position advocated by Respondents will only exacerbate these problems and proliferate more of these "blackmail settlements." *Rhone*, *supra* at 1298, citing Henry J. Friendly, *Federal Jurisdiction: A General View* 120 (1973).

This Court should reverse the decision below to adhere to the plain language of the SLUSA requirements that covered class actions alleging only 1933 Act claims must be adjudicated in federal court. Congress intended to – and did – confer a statutory right on defendants to present their defenses to such claims in a federal forum. Plaintiffs and their lawyers should not be permitted to circumvent the protections that the SLUSA provided to defendants. But if this Court adopts Respondents' argument, this is exactly what will occur. In turn, this will allow

abusive class actions to progress more easily at the state court level to certification – and legally unwarranted settlement. And the enhanced promise of a pay-off would trigger the filing of many more strike suits brought by opportunistic plaintiffs' attorneys to obtain "the defendants' cost savings from avoiding the litigation, distraction, and reputation costs of responding to the plaintiffs' complaint" rather than the true worth of the claim. James Bohn & Stephen Choi, *Fraud in the New-Issues Market: Empirical Evidence on Securities Class Actions*, 144 U. Pa. L. Rev. 903, 970 (1996).

CONCLUSION

For the foregoing reasons, the Court should reverse the decision of the Court of Appeal of the State of California, First Appellate District.

Respectfully submitted,

JOHN E. CUTTINO
President of DRI— The Voice of the Defense Bar
55 W. Monroe St.
Suite 2000
CHICAGO, IL 60603

MARY MASSARON
Counsel of Record
HILARY A. BALLENTINE
PLUNKETT COONEY
38505 Woodward Avenue
Suite 100
Bloomfield Hills, MI 48304
(248) 901-4000
mmassaron@plunkettcooney.com

Counsel for Amicus Curiae DRI – The Voice of the Defense Bar

August 31, 2017